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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of

Price Cap Regulation of
Local Exchange Carriers

Rate of Return Sharing
And Lower Formula Adjustment

CC Docket No. 93-179

COMMENTS

OF

THE SOUTHERN NEW ENGLAND TELEPHONE COMPANY

The Southern New England Telephone Company (SNET) respectfully submits its Comments pursuant to the Federal Communication Commission's (Commission's) Notice of Proposed Rulemaking, (NPRM) released July 6, 1993.¹

In the NPRM, the Commission proposes to include the effects of an "add-back" adjustment on rate of return calculations for the purposes of the backstop sharing and lower formula adjustment (LFAM) for local exchange carriers (LECs) subject to price cap regulation.² In these Comments, SNET agrees with the Commission's conclusion that such an add-back of the lower formula adjustment is necessary to maintain the proper relationship between rate of return and

¹ In the Matter of Price Cap Regulation of Local Exchange Carriers; Rate of Return Sharing and Lower Formula Adjustment, CC Docket No. 93-179, Notice of Proposed Rulemaking, FCC 93-325, released July 6, 1993 (NPRM).

² NPRM at para 4.

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performance in a prior year.³ SNET also agrees that, without add-back, artificial swings in earnings can occur that effectively double-count the amount of the backstop adjustment, once in the base year and then again in the tariff year.⁴

1. Add-back of the lower formula adjustment is necessary to properly relate rate of return to performance in a prior period.

SNET's 1992 Annual Access tariff filing included a lower formula adjustment amount resulting from interstate Price Cap earnings of less than the lower formula adjustment mark of 10.25%.⁵ Then, in SNET's 1993 Annual Access tariff filing, SNET excluded its 1992 LFAM revenues from 1992 earnings to comply with the Commission's LEC Order on Reconsideration.⁶ SNET reversed the LFAM rate increase in its 1993 Annual Access tariff filing by taking a negative exogenous change in the price cap index for the entire LFAM amount.⁷ SNET correctly eliminated the effect of the LFAM by subtracting the LFAM revenue from 1992 earnings prior to determining the rate of return for ratemaking.⁸

³ NPRM at para. 11.

⁴ NPRM at para. 12.

⁵ See SNET 1992 Annual Access Tariff Filing, Transmittal No. 538, Volume 1 of 2, filed April 2, 1992.

⁶ LEC Price Cap Reconsideration Order, 6 FCC Rcd 2637 at fn. 166.

⁷ See Reply Comments of SNET, 1993 Annual Access Tariff Filing, Transmittal No. 560, at page 4, filed May 10, 1993. ("Reply Comments")

⁸ See SNET's 1993 Annual Access Tariff filing, Volume 2 of 2, Section 2, Workpaper 492A 1992-3, "Adjustment to 1992 Results for Low End Amount," filed April 2, 1993.

2. Failure to remove the temporary effect of the lower formula adjustment amount would result in incorrect PCI and earnings swings.

SNET agrees with the Commission that, without add-back, there can be artificial swings in earnings. As part of its 1993 Annual Access Tariff filing, SNET first reduced rates in the price cap index (PCI) by reversing the effect of the LFAM amount, and then determined if a further reduction in rates was necessary by an analysis of the rate of return.⁹ Because the PCI had already been reduced for the reversal of the LFAM amount, the 1992 earnings price level rate of return test would have double-counted the impact of the LFAM if the 1992 rate of return had not been adjusted to remove the LFAM revenues. If earnings were not adjusted for the LFAM revenues, then SNET would have incorrectly lowered its rates twice -- once in the PCI for the reversal of the LFAM, and again due to the impact on 1992 earnings, of the same LFAM amount. In support of this point, SNET provided an example to demonstrate the correct and incorrect procedure for LFAM reversal.¹⁰

⁹ See Direct Case of SNET in Response to Issues Designated for Investigation, 1993 Annual Access Tariff Filing, CC Docket No. 93-193, filed July 27, 1993, at pp 7 - 8.

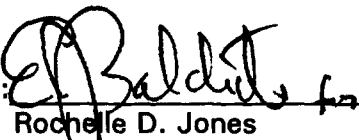
¹⁰ See Reply Comments at Attachment A.

Conclusion

For the reasons stated above, SNET supports the Commission's conclusions about utilizing an add-back adjustment as part of the rate of return calculation for the lower formula adjustment mechanism. Further, such an add-back adjustment is consistent with the LEC price cap plan as adopted by the Commission.

Respectfully submitted,

THE SOUTHERN NEW ENGLAND TELEPHONE COMPANY

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